

MAY 08 2006

BEFORE THE FEDERAL ELECTION COMMISSION

In the Matter of

Joe Turnham for Congress and Pete Turnham
in his official capacity as treasurer; Joseph R. Turnham;
Pete Turnham; and BancorpSouth Bank

MUR 5685

SENSITIVE

GENERAL COUNSEL'S REPORT # 2

I. ACTIONS RECOMMENDED:

Take no further action with respect to BancorpSouth Bank and close the file as to this Respondent; take no further action with respect to Joe Turnham for Congress and Pete Turnham in his official capacity as treasurer ("the Committee") and Joseph R. Turnham in connection with the bank loan

II. BACKGROUND

The Commission previously found, *inter alia*, reason to believe that BancorpSouth, the Committee and Joseph R. Turnham violated 2 U.S.C. § 441b(a) in connection with three loans the bank made to the Committee from about May to October 2002 totaling \$98,023.¹ See First General Counsel's Report, October 28, 2005. The basis for the Commission's finding was information contained in the Final Audit Report ("FAR") for the Committee referred to the

¹ With the exception of an excessive contribution made by Pete Turnham, all of the facts in this matter occurred prior to the effective date of the Bipartisan Campaign Reform Act of 2002 ("BCRA"), Pub. L. 107-155, 116 Stat. 81 (2002). Accordingly, unless specifically noted to the contrary, all citations to the Federal Election Campaign Act of 1971, as amended ("the Act"), herein are as it read prior to the effective date of BCRA and all citations to the

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1 General Counsel's Office for enforcement. The FAR showed, among other things, that the bank
2 loans did not appear to be made on a basis that assured repayment because the loans were not
3 perfected with a security interest in collateral and lacked a pledge of future receipts or income.
4 *See FAR (A03-05), Finding 2. Receipt of Unsecured Bank Loans.*

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10 During the investigation, the bank voluntarily provided affidavits from David S. Adcock,
11 First Vice-President at BancorpSouth, and supporting loan documentation, which appear to
12 establish that the bank loans were made on a basis that assures repayment when considering the
13 case-by-case option provided for by the Commission's regulations.² *See* 11 C.F.R.
14 § 100.7(b)(11)(ii); *see also* Advisory Opinion 1994-26 (September 26, 1994); *see also*
15 Explanation and Justification for Regulations on Loans From Lending Institutions to Candidates
16 and Political Committees, 56 Fed. Reg. 67118, 67119-67121 (Dec. 27, 1991).

Commission's regulations herein are to the 2002 edition of Title 11, Code of Federal Regulations, which was published prior to the Commission's promulgation of any regulations under BCRA.

² Mr. Adcock has 21 years of experience in the banking industry including loan administration and credit analysis. Adcock Aff., January 27, 2006. He joined BancorpSouth in 1991 and worked at various posts, including Assistant Vice-President and Commercial Loan Officer; Vice-President, Credit Analyst and Underwriter for Loan Administration; Manager of Asset Based Lending, and Regional Loan Administrator. *Id.* As a Regional Loan Administrator, he was responsible for review of loan approvals which exceeded the lending limit of the local bank presidents and for overall loan quality. *Id.* After reviewing all the pertinent loan documentation, as well as Joe Turnham's credit report from the relevant time period, he assisted BancorpSouth's counsel in the preparation of the letters attached to his affidavits and affirmed the contents thereof. Adcock Aff., December 21, 2005 and January 27, 2006

III. DISCUSSION

During the investigation, the bank submitted copies of, among other things, the Commercial Loan Applications and the accompanying Unconditional and Continuing Guaranty for each loan.³ Attachment 2. According to the documentation, BancorpSouth made three loans to the Committee as follows:

	Amount	Date	Maturity Date	Date Repaid
Loan A	\$20,075	5/28/02	8/26/02	10/15/02
Loan B	\$17,075	6/17/02	9/15/02	10/15/02
Loan C	\$60,0873	10/15/02	1/13/03	2/5/03

Id.; see also First General Counsel's Report, October 28, 2005; see also FAR (A03-05), *Finding 2. Receipt of Unsecured Bank Loans*. The recipient of each of the loans was the Committee. *Id.* It is undisputed that the loan proceeds were used for Joe Turnham's campaign expenses related to his 2002 campaign for Congress. *Id.* Joe Turnham personally guaranteed each of the loans with his signature. *Id.*

The Act prohibits national banks from making contributions in connection with any federal election and prohibits candidates, political committees, or other persons from knowingly

³ The bank's retention policies did not require it to keep the guaranty documents on file once the loan was repaid Adcock Aff Ex A at 3, December 21, 2005. The bank's technical staff "recreated" the guaranty documents as they would have appeared during the relevant time period. *Id.*

1 accepting or receiving such contributions. 2 U.S.C. § 441b(a). The term "contribution" does not
2 include a loan from a qualifying bank if such loan is made in accordance with applicable banking
3 law and regulations and is made in the ordinary course of business.⁴ 2 U.S.C. § 431(8)(B)(vii);
4 11 C.F.R. § 100.7(b)(11). The BancorpSouth loans were not secured with direct collateral, or the
5 pledge of future receipts or income.⁵ Attachment 2; *see also* First General Counsel's Report,
6 October 28, 2005; *see also* FAR (A03-05), *Finding 2. Receipt of Unsecured Bank Loans*.
7 Commission regulations provide that absent a perfected security interest or pledge of future
8 receipts, loans can be guaranteed by the borrower's signature based on the "totality of the
9 circumstances on a case-by-case basis." *See* 11 C.F.R. § 100.7(b)(11)(ii); *see also* Advisory
10 Opinion 1994-26 (September 26, 1994); *see also* Explanation and Justification, Loans from
11 Lending Institutions to Candidates and Political Committees, 56 Fed. Reg. 67118 (Dec. 27,
12 1991).

13 In reviewing the totality of the circumstances regarding assurance of repayment, a number
14 of factors are evaluated in determining whether the bank could expect a loan to be repaid,
15 including the borrower's financial situation (e.g., income and credit background), the borrower's
16 pre-existing relationship to the lending bank, and the terms of the loan. *See* Advisory Opinion
17 1994-26; *see also* MURs 5198 (Cantwell 2006) and 5262/5266 (Tim Ryan for Congress).

⁴ A loan is considered to be made in the ordinary course of business if it: (1) bears the usual and customary interest rate of the lending institution for the category of loan involved; (2) is made on a basis which assures repayment; (3) is evidenced by a written instrument; and (4) is subject to a due date or amortization schedule. 11 C.F.R. § 100.7(b)(11).

⁵ A borrower can meet the Commission's standard for assurance of repayment of a loan, if: (1) the lending institution has perfected a security interest in collateral owned by the candidate or political committee receiving the loan, and the fair market value of the collateral is equal to or greater than the loan amount; or (2) the lending institution has obtained a written agreement whereby the candidate or political committee receiving the loan has pledged future receipts, e.g., public financing funds, contributions, and interest income; or (3) a combination of (1) and (2). 11 C.F.R. § 100.7(b)(11)(i)(A) and (B).

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1) The Candidate's Creditworthiness Was Evaluated by BancorpSouth at the Time of the Original Loan Application.

According to Mr. Adcock, "[t]he information contained in the loan applications, when viewed in the context of the bank's appetite for credit risk, Mr. Turnham's reputation in the community and the bank's experience with his accounts and loans in the past adequately supported the credit decisions to approve the loans at the stated rates and terms as requested by Mr. Turnham." Adcock Aff. Ex. A ¶ 2, January 27, 2006.

The size and category of the loans involved were within the local community bank's lending authority. Adcock Aff. Ex. A at 2, December 21, 2005. The local branch officer performed the credit review process at the origination of the loan, and the Regional and Divisional Loan Committees thereafter approved the loans.⁶ *Id.* The application for the May 2002 loan lists Mr. Turnham's total assets total liabilities and net worth as of a financial statement dated January 11, 2000. Attachment 2 at 1. Information regarding Joe Turnham's credit score debt to income ratio income and liquidity also appear on the face of the loan application. *Id.*

As noted on the loan application, Mr. Turnham's 2002 credit report and history was considered: "CBI reflects 2 GMAC loans rated 1-2 in April of 2002. All rest of credit is satisfactory. We have granted several loans of this type to Mr. Turnham. Updated financial statement requested." *Id.* According to Mr. Adcock, the notations regarding the GMAC loans mean that all loans on Joe Turnham's credit history were paid as agreed except for two GMAC loans – one was past due for 30 days, "...but reviewing the history as detailed on the credit

⁶ Some of the loan applications contain the divisional and regional loan committee approval stamps Attachment 2 at 1 – 5 Given the bank's submission, we have no reason to doubt its contention that its usual and customary review process was conducted with respect to all three loans

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1 report, the past due was not excessive and overall the credit had [sic] paid satisfactorily. The
2 second loan . . . [was] paid off and reported to be 'Closed Normally'; therefore, after showing
3 past due [,] the credit was paid in its entirety." Adcock Aff. Ex. A ¶ 3, January 27, 2006.

4 On October 15, 2002, Joe Turnham provided the bank with an updated financial
5 statement as requested. "Upon comparison to the previous financial statement furnished, no
6 material changes were noted that would affect the credit relationship that Mr. Turnham currently
7 maintained with BancorpSouth Bank."⁷ *Id.*

8 According to the bank's submission, Joe Turnham repaid approximately \$2,000 towards
9 the May and June 2002 loans, and it looked upon this information favorably before it considered
10 extending the October 2002 loan to him. Adcock Aff. Ex. A at 2, December 21, 2005; *see also*
11 Attachment 2 at 3.

12 **2) *BancorpSouth Had a Pre-existing Banking Relationship with the Candidate***
13 ***Prior to the Extension of Credit in 2002.***
14

15 BancorpSouth alleges that it "has a true community bank style," and that it considered Joe
16 Turnham to have an "inherited" relationship, in that Mr. Turnham's relationship predated
17 BancorpSouth's acquisition of the former First National Bank of Opelika, Alabama.⁸ Adcock
18 Aff. Ex. A at 1, December 21, 2005. The "community banking" style of the bank means a
19 family's past dealings with the bank weigh considerably in making a decision as to whether or
20 not to approve a loan to a borrower. Adcock Aff. Ex. A at 2, December 21, 2005. According to
21 Mr. Adcock, the "... concepts of relationships and 'knowing your customer' are critical to

⁷ The October 2002 loan application lists Joe Turnham's updated financial information as follows: total assets
total liabilities and net worth His credit rating is listed income
debt to income ratio and liquidity Copies of both the January 11, 2000 and October
15, 2002 financial statements were provided by the bank as part of its submission.

⁸ BancorpSouth merged with First National Bank of Opelika in 1998. *See*
http://www.findarticles.com/p/articles/mi_m0EIN/is_1998_Dec_31/ai_53496664

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1 community banking.” *Id.* “[T]he Turnham family had quite a longstanding and valuable
2 relationship” with the bank. *Id.*

3 “[T]he credit relationship with Joe Turnham was a normal loan relationship as
4 compared to a customer with his type [of] established pay history with First National, then
5 BancorpSouth, coupled with a historically favorable family relationship.” *Id.* According to Mr.
6 Adcock, at the time of the May 2002 loan application the bank also took into consideration Joe
7 Turnham’s previous loan history with the bank and the approximately \$30,000 he repaid towards
8 those preexisting loans.⁹ Adcock Aff. Ex. A at 3, December 21, 2002.

9 “[I]f as was true with Joe Turnham and his family, they had successfully met credit
10 obligations to First National and this bank in the past, [then] a community banker is much more
11 prone, in the ordinary course to extend loans to borrowers withoutmore ‘traditional’
12 collateral. Such is true with Mr. Turnham.”¹⁰ Adcock Aff. Ex. A at 2, December 21, 2005. We
13 have no reason to doubt the bank’s contention that Joe Turnham’s treatment was typical of its
14 relationships with numerous other community customers.¹¹

⁹ All the available information suggests that the previous loan history was in connection with Joe Turnham’s 1998 campaign for Congress, as opposed to Joe Turnham’s personal use. See FAR (A03-05), *Finding 2. Receipt of Unsecured Bank Loans*.

¹⁰ The deposits Joe Turnham had on account with the bank in 2002 contained insufficient balances to secure the loans. See FAR (A03-05), *Finding 2. Receipt of Unsecured Bank Loans*. However, we believe the supporting loan documentation shows that Joe Turnham had sufficient income and other assets to assure repayment of the loans. Attachment 2.

¹¹ We do note that Tim Turnham (Joe Turnham’s brother) served on the BancorpSouth Opelika advisory board. The bank explained that “[...]his is truly a business development group, non-decision-making, with no authority to act or otherwise bind the company.” *Id.* The investigation uncovered no information suggesting that Tim Turnham’s position on the bank’s advisory board unduly influenced the bank’s decision to approve the 2002 loans to the Committee.

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1 **3) The Terms of the Loans do not Appear to be Out of the Ordinary or Unduly**
2 **Favorable to the Candidate.**

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4 The loans contained an 8% interest rate, which “constitute[d] ‘market rates’ during the
5 relevant time frame.” Adcock Aff. Ex. A at 2, December 21, 2005. According to Mr. Adcock,
6 the loans were in the category of “not otherwise secured,” rather than unsecured, the distinction
7 being that the loans are secured by the continuing guarantees of Joe Turnham and are subject to
8 setoff rights to deposit accounts.¹² Adcock Aff. Ex. A at 3, December 21, 2005; *see also*
9 Attachment 2.

10 According to Mr. Adcock, these types of “not otherwise secured” loans were “not
11 specialized or unique” to Mr. Turnham, but “can be quite routine in the BancorpSouth system.”
12 *Id.* As an example, BancorpSouth alleges that it currently maintains a portfolio of “not otherwise
13 secured loans” consisting of over 16,000 loans totaling over \$442,000,000.00. *Id.* “Taking these
14 ‘not otherwise secured’ loans in the ranges affiliated with the Turnham credits, namely in the
15 \$15,000 to \$75,000.00 range, (in relation to the total outstanding loans guaranteed by Joe
16 Turnham), over \$65,000,000.00 of loans fall in such category, representing over 2100 ‘not
17 otherwise secured’ loans.”¹³ *Id.*

18 It was BancorpSouth’s usual lending practice to extend this category of loan for
19 “relatively short terms”, as it did in Mr. Turnham’s case. *Id.* The 3-month term of the loan
20 “allows the bank to... manage credits and manage interest rates and pricing, and otherwise

¹² See discussion at footnote 10 *supra*.

¹³ These statistics represent BancorpSouth’s 2005 loan portfolio. Adcock Aff Ex A ¶ 5, January 27, 2006. According to the bank, its programmers had the ability to generate the report by loan codes that identify “not otherwise secured” loans related to the loan portfolio at the time of the request. However, according to the programmers, the loan data for 2002 is not available in a format to generate the same report. *Id.* Given the proximity of the dates, Mr. Adcock’s tenure with the bank, and the lack of information indicating otherwise, we accept Mr. Adcock’s assertion that the 2005 portfolio mirrors the bank’s 2002 portfolio

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1 monitor such loans..." *Id.* It was the bank's "normal course" that "short term financing
2 becomes renewed and extended as opposed to being considered 'matured' and paid." Adcock
3 Aff. Ex. A at 3 - 4, December 21, 2005. The application for the June 2002 loan contains the
4 following notation: "Loan to be paid off prior to maturity. Will term out if not P/O at maturity."
5 Attachment 2 at 3. The application for the October 2002 loan contains the following notation:
6 "This loan represents a refinance of #34400162874 & 344000158209 plus \$26,700 in new
7 money. At maturity this loan will be collateralized [sic] and amortized. We will also require a life
8 insurance policy as additional collateral. The customer pd \$2,051 to principal plus interest."
9 Attachment 2 at 5. According to Mr. Adcock's submission, these terms, e.g., the prospect of
10 renewals, or if not renewed, to be termed out, with the possibility of being collateralized if placed
11 on longer terms, were "all in the normal course." Adcock Aff. Ex. A at 4, December 21, 2005.

12 Although the October 2002 loan was repaid 23 days late (the maturity date was January
13 13, 2003 and the loan was repaid on February 5, 2003), the bank did not consider the loan to be
14 in default. *Id.* "...[T]o either the local bankers or up the management chain, a loan less than 30
15 days past due, especially when one is dealing with a customer based on prior successful pay
16 downs, is simply not on the radar screen of being considered in default." *Id.* Furthermore,
17 according to Mr. Adcock's submission, a loan of this size in the category of "not otherwise
18 secured" would not be criticized by the FDIC for slightly exceeding the original due date.
19 "Loans of this type even have the equivalent of a built-in grace period mechanism by way of the
20 late charge provision. Stated differently, a loan at BancorpSouth which matured mid-month and
21 was paid off a couple of weeks later (for which interest continued to accrue post-maturity until
22 paid) would not be unusual." Adcock Aff. Ex. A at 4, December 21, 2005.

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1 In sum, the investigation has uncovered no evidence indicating that the terms and
2 treatment of the loans were in any way preferential. We therefore conclude that based on the
3 totality of circumstances, discussed *supra*, BancorpSouth intended to assure repayment and
4 properly approved the loans to the Committee as guaranteed by Joe Turnham's signature.
5 Accordingly, we recommend that the Commission take no further action with respect to
6 BancorpSouth Bank, Joe Turnham for Congress and Pete Turnham in his official capacity as
7 treasurer, and Joseph R. Turnham in connection with the bank loan.

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V. **RECOMMENDATIONS**

1. Take no further action with respect to BancorpSouth Bank and close the file as to this respondent.
2. Take no further action with respect to Joe Turnham for Congress and Pete Turnham in his official capacity as treasurer in connection with the bank loan.

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3. Take no further action with respect to Joseph R. Turnham in connection with the bank loan.

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7. Approve the appropriate letters.

Lawrence H. Norton
General Counsel

5/8/06
Date

BY:

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Attachments

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